

Federal Bank

BUY

Strong credit growth; Asset quality remain stable

Summary

Federal Bank credit growth remained strong at 19 YoY (vs 20% YoY Q1FY25) led by growth across the segments. Deposits growth declined to 16% YoY vs 20% YoY (Q1FY25) led by NRE deposits. We expect 18% CAGR (FY24-26) credit growth. NIMs declined by 4bps QoQ during Q2FY25 led by accounting of penal interest charges however, guided for stability in next 2 quarters. Asset quality remains stable with GNPA at 2.09% vs 2.11% QoQ. NII grew by 15% YoY; higher provisions (up 2.6x YoY) impacted the profitability growth (up 11% YoY). This resulted RoA to 1.28% (1.27% Q1FY25). Management guided RoA to remain at ~1.3% levels for FY25. We have largely maintained estimates and maintain BUY rating with the target price of Rs.240 based on 1.6x P/ABV FY26.

Key Highlights and Investment Rationale

- Strong credit growth:** Loan book grew by 19% YoY (up 4% QoQ) as against 20% YoY (Q1FY25). Retail/Agri/SME grew at 17% YoY/14% YoY/19% YoY respectively, whereas corporate book grew by 10% YoY. Deposits growth declined to 16% YoY vs 20% YoY (Q1FY25) as NRE deposits slowdown.
- Asset quality stable; slippage ratio remains stable:** Asset quality stable as GNPA stood at 2.09% vs 2.11% QoQ and NNPA at 0.57% vs 0.6% QoQ. Slippage ratio remains stable at 0.8% vs 0.8% QoQ.
- NIMs declined by 4bps QoQ:** NIMs declined by 4bp QoQ to 3.12% led by change in regulatory requirement of penal charges during the quarter. Cost to income ratio remain stable at 53% vs 53% QoQ.
- Outlook:** The bank's focus on the higher margin products by leveraging on its digital, analytical and branch lite partnership based model should support higher return ratios. With new management, will watch out for strategy and focus area for long term. We expect RoA to sustain at higher levels (~1.3%).

TP Rs.240

CMP Rs.185

Potential upside/downside 30%

Previous Rating BUY

Price Performance (%)

	-1m	-3m	-12m
Absolute	(4.5)	(6.8)	32.4
Rel to Sensex	2.0	(5.1)	6.9

V/s Consensus

EPS (Rs)	FY25E	FY26E
IDBI Capital	16.8	20.3
Consensus	17.1	20.1
% difference	(1.6)	0.9

Key Stock Data

Bloomberg / Reuters	FB IN / FED.BO
Sector	Banking
Shares o/s (mn)	2,453
Market cap. (Rs mn)	452,998
3-m daily avg trd value (Rs mn)	94.4
52-week high / low	Rs207 / 137
Sensex / Nifty	80,005 / 24,339

Shareholding Pattern (%)

Promoters	0.0
FII	27.7
DII	44.5
Public	27.8

Financial snapshot

(Rs mn)

Year	FY2022	FY2023	FY2024	FY2025E	FY2026E
NII	59,620	72,322	82,935	96,676	1,14,669
Change (yoy, %)	8%	21%	15%	17%	19%
Net Profit	18,898	30,106	37,206	41,073	49,699
Change (yoy, %)	19%	59%	24%	10%	21%
EPS (Rs)	9.0	14.2	15.3	16.8	20.3
Change (yoy, %)	13%	58%	7%	10%	21%
ABV (Rs)	84.4	97.4	115.6	130.8	147.8
PER (x)	20.6	13.0	12.1	11.0	9.1
P/ABV (x)	2.2	1.9	1.6	1.4	1.3
ROE (%)	10.8	14.9	14.7	13.2	14.0
ROA (%)	0.9	1.3	1.3	1.2	1.3
GNPA (%)	2.8	2.4	2.1	2.1	2.2
NNPA (%)	1.0	0.7	0.6	0.7	0.7
CAR (%)	15.8	14.8	16.1	14.7	14.3

Source: IDBI Capital Research

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Conference Call Highlights

Operational Performance

- The total business of the bank reached Rs.4994.2bn with the last Rs.1000bn added in last four quarters.
- The bank achieved the highest ever net profit of Rs.10.6bn, reflecting a growth of 10.8% YoY.
- The two new corporate partners (Tata AIA and Bajaj Allianz Life) has given more distribution capability for the bank resulting in higher income.
- The impact of penal charges on NIM is about 7 bps this quarter.
- The average LCR during the quarter stood at 115%.

Advances and Deposits

- The management said that the bank will continue to pursue loan growth where there is a growth opportunity, without impacting asset quality.
- The bank introduced a new scorecard for personal loan segment, which resulted in lower disbursements. However, the bank benefitted from this new process in the form of controlled slippages.
- While the industry approval for MFI loans is at 45%, the bank's approval rate stood at 33%, reflecting conservative stance. There is no top up loan in this segment.
- The bank is complying with all the norms pertaining to fair gold loan practices.
- The share of gold loans sourced from fintechs is about 10% of the gold loan portfolio.
- The share of unsecured loan is about 4.6% of the total advances.
- The branch banking business remained a strong contributor to the granular deposit growth, demonstrating improved accretion despite a challenging deposit environment.
- The bank achieved the strong deposit growth without significant concessions on deposit rates, diverging from the broader industry trend of elevated rates.

- The bank has been able to maintain the CASA growth momentum in Q1 and Q2, and the primary focus remains on ensuring that it gets a primary bank status with both new and existing customers.
- The bank has calibrated the costs on term deposit that would prevent them from paying abnormally high rates.
- The remittance volumes have gone up in non-resident savings bank account quarter on quarter. The bank increased the pace of number of accounts opened including in Middle East, added few more capabilities and increased the number of relationship managers.
- The bank looked at opportunities outside GCC Kerala corridor and increased NR branches and presence.

Asset Quality

- The company has cautious on the high margin products, including the MFI products, due to the asset quality issues.
- While the bank has seen higher slippages from MFI, the bank has been able to control slippages because of the states in which it operates (More than 2/3rd of this portfolio is in South India).
- The bank witnessed a slight uptick in slippage rates for both credit cards and personal loan segments, sourced through organic as well as partners. However, the share in the overall portfolio remains small.
- The bank saw better-than-expected slippages on home loans, car loans, and vehicle loans.
- The bank expects issues in the MFI segment to stabilise in the next two quarters. The bank does not expect significant uptick in slippages going ahead.

Guidance

- The bank is placing a renewed focus on CASA and deposit growth, supported by the newly secured AAA rating on the deposit program.
- The bank expects core fee income to witness an improving trend in the coming quarters.
- The bank maintains its credit growth guidance of ~18% going ahead.
- The management expects the opex in H2 to remain at similar level like in H1 of the current financial year.

- The management expects ROA to be around ~1.8% and ROE to be ~13.5% levels for FY25.
- The bank will evaluate its portfolio to improve the NIM going forward.
- The bank maintained its credit cost guidance of ~30-35 bps for FY25.
- The bank is looking to raise funds via infrastructure bonds in the near term.
- On the RBI embargo on co-branded credit card, the bank is actively working with all the partners to ensure compliance.
- The bank is reviewing and working on complying with all the regulations on the model which it has with Scapia. On the other hand, the bank's OneCard may take longer time for compliance with the RBI norms.

Other Key Highlights

- The new MD and CEO KVS Manian has been conducting deep dive sessions with each business unit and functions to understand the current position and identifying growth opportunities.
- CEO Manian also met with customers, key stakeholders and partners, and he plans to complete the structured outreach program by around mid-November to third week of November.
- The new chief will present to the board in December with the various strategies after getting an understanding of the business.

Exhibit 1: Quarterly Snapshot

(Rs mn)

Year-end: March	Q2FY25	Q2FY24	Q1FY25	YoY (%)	QoQ (%)
Interest Income	65,773	54,553	63,309	20.6	3.9
Interest Expenses	42,101	33,989	40,389	23.9	4.2
Net Interest Income	23,672	20,564	22,920	15.1	3.3
NIM (%)	3.12	3.22	3.16	-10 bps	-4 bps
Non-Interest Income	9,640	7,304	9,152	32.0	5.3
Operating Income	33,312	27,868	32,072	19.5	3.9
Staff Cost	7,777	6,263	7,380	24.2	5.4
Other Op Exp	9,882	8,361	9,682	18.2	2.1
Total Operating Expenses	17,658	14,624	17,063	20.7	3.5
<i>Cost to Income (%)</i>	<i>53.0</i>	<i>52.5</i>	<i>53.2</i>	<i>53 bps</i>	<i>-19 bps</i>
Operating Profit	15,654	13,245	15,009	18.2	4.3
Provisions	1,584	439	1,443	260.7	9.8
PBT	14,070	12,806	13,566	9.9	3.7
Tax	3,503	3,267	3,471	7.2	0.9
<i>- effective tax rate</i>	<i>24.9</i>	<i>25.5</i>	<i>25.6</i>	<i>-62 bps</i>	<i>-69 bps</i>
PAT	10,567	9,538	10,095	10.8	4.7
EPS (Rs)	4.3	4.1	4.1	6.2	4.6
BV (Rs)	128.3	111.1	124.8	15.5	2.8
Deposits	26,91,066	23,28,684	26,60,650	15.6	1.1
Advances	23,03,122	19,28,167	22,08,070	19.4	4.3

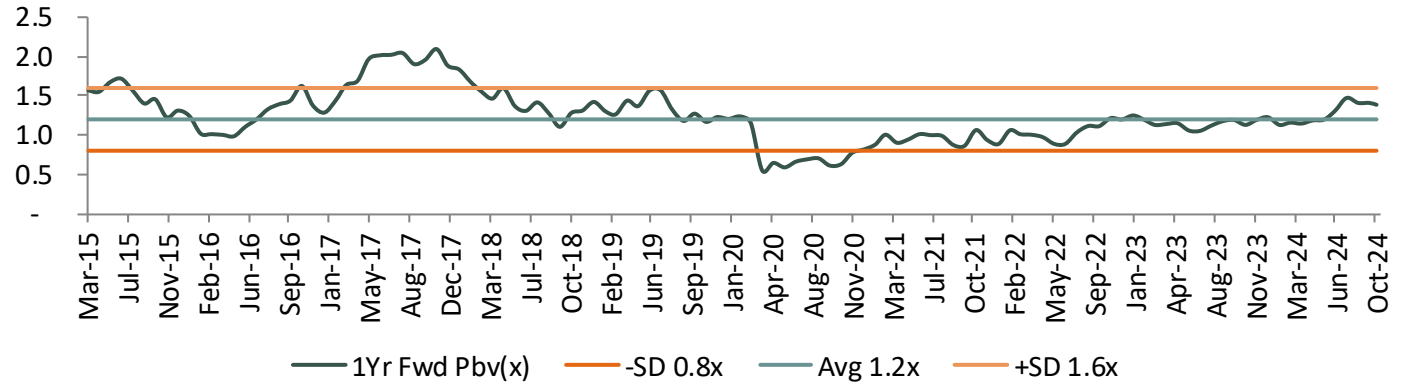
Source: Company; IDBI Capital Research

Exhibit 2: ROE Decomposition

(%)	FY22	FY23	FY24	FY25E	FY26E
NII	2.8	3.0	2.9	2.9	2.9
Fees	0.8	1.0	1.0	0.9	0.9
Other Income	0.1	0.0	0.1	0.2	0.2
Net Revenue	3.8	4.0	4.0	4.0	4.0
Op.Exp	2.0	2.0	2.2	2.1	2.1
Op.Profit	1.8	2.0	1.8	1.8	1.9
Provisions	0.6	0.3	0.1	0.2	0.2
PBT	1.2	1.7	1.8	1.6	1.7
Tax	0.3	0.4	0.4	0.4	0.4
ROA	0.9	1.3	1.3	1.2	1.3
Leverage (x)	12.1	11.9	11.2	10.8	11.1
ROE	10.8	14.9	14.7	13.2	14.0

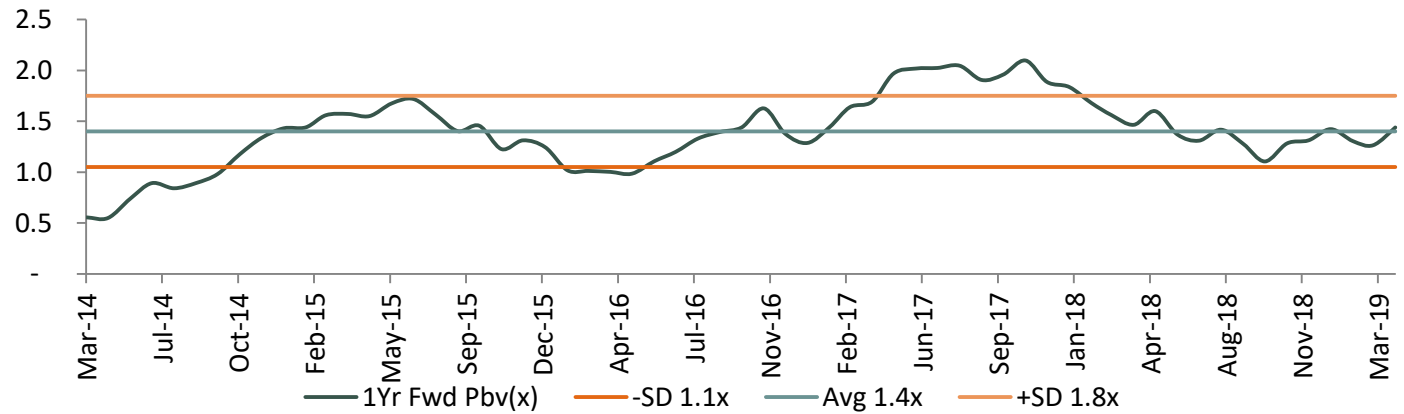
Source: Company; IDBI Capital Research

Exhibit 3: One-year forward P/ABV (FY15-FY25)



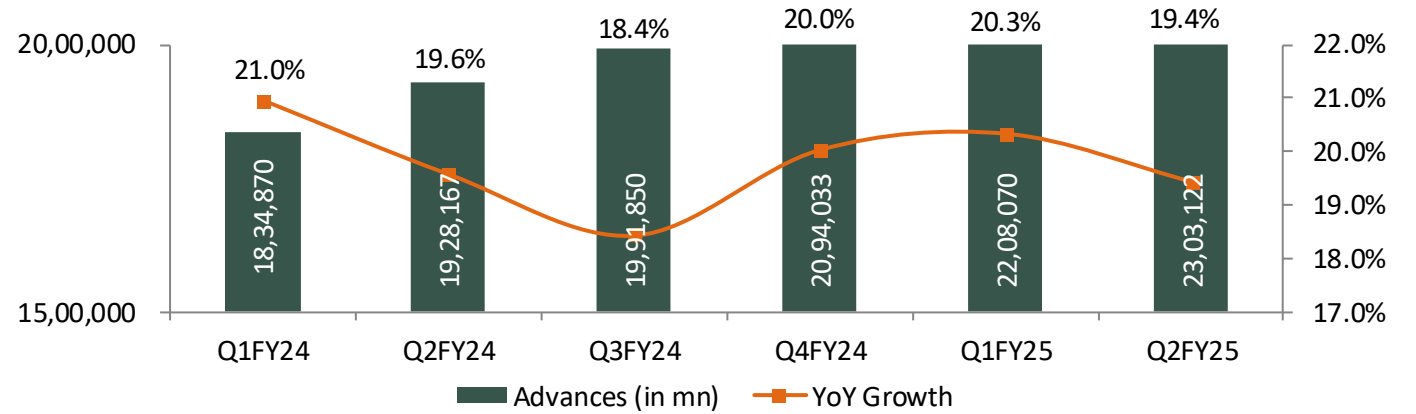
Source: Company; IDBI Capital Research

Exhibit 4: One-year forward P/ABV (FY14-FY19)



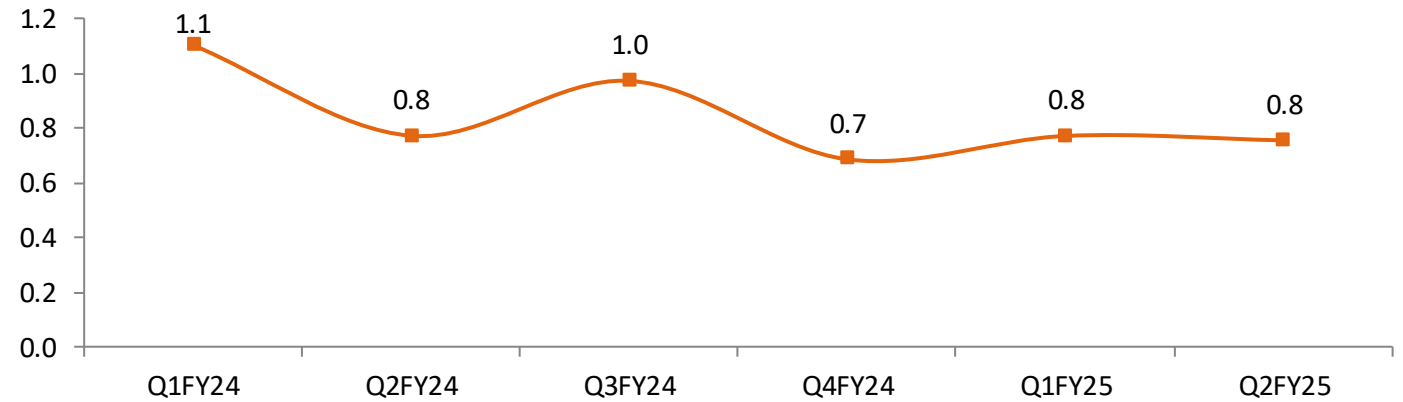
Source: Company; IDBI Capital Research

Exhibit 5: Advances growth continued to witness strong growth momentum on YoY basis



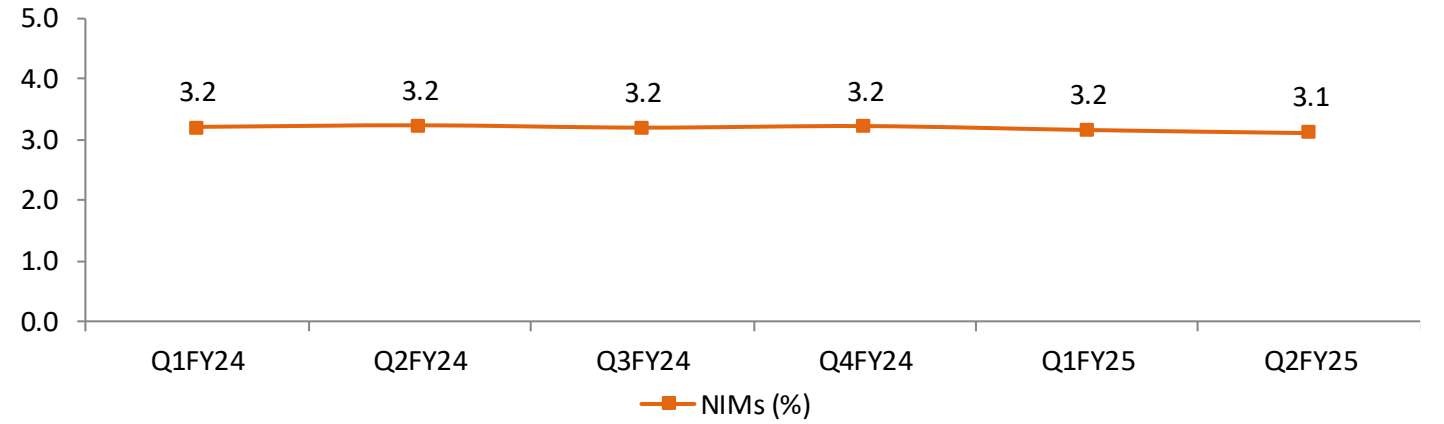
Source: Company; IDBI Capital Research

Exhibit 6: Slippage ratio remained stable sequentially



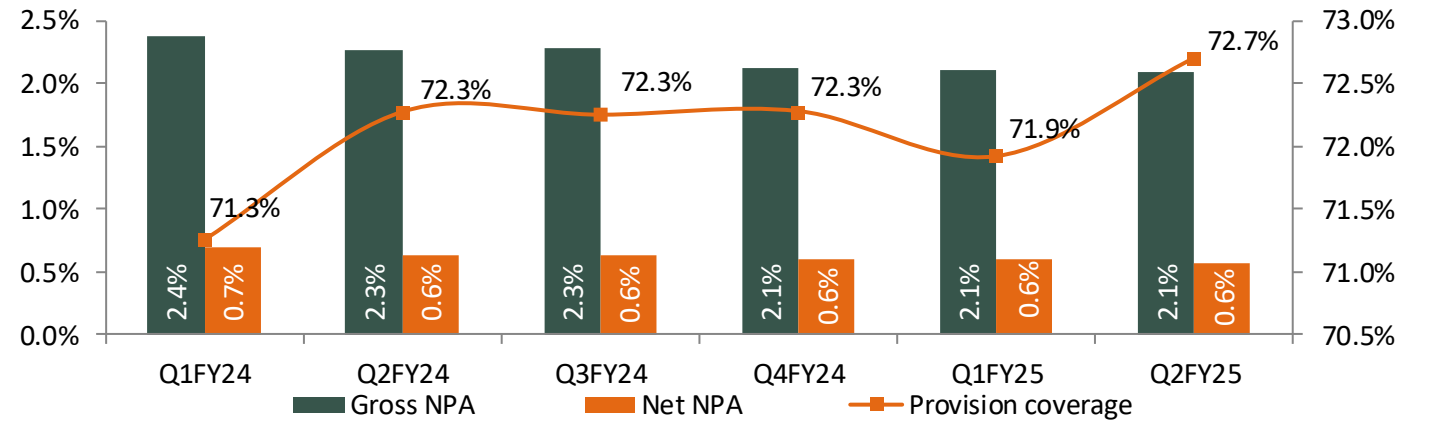
Source: Company; IDBI Capital Research

Exhibit 7: Net Interest margins slightly declined QoQ



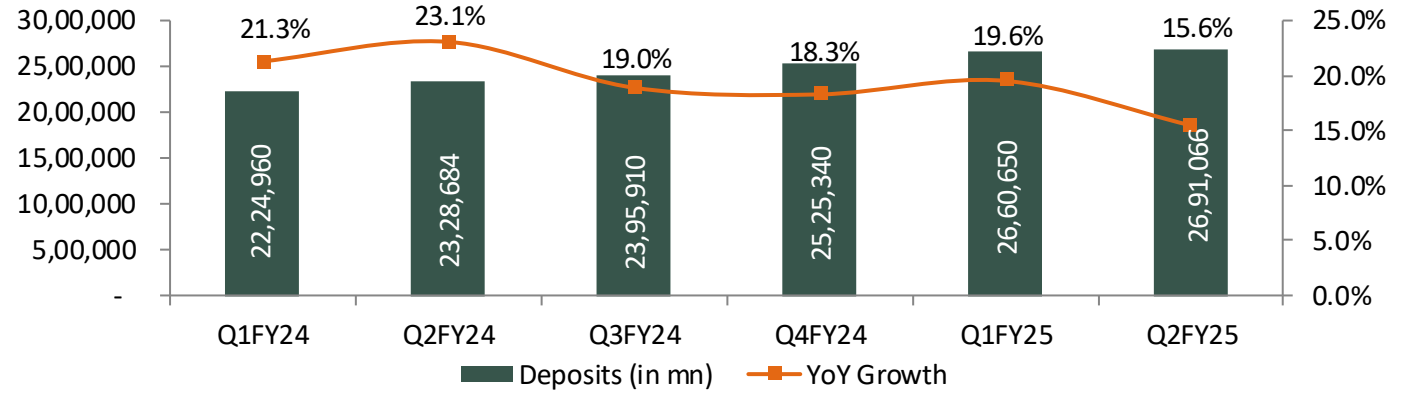
Source: Company; IDBI Capital Research

Exhibit 8: Asset quality remained stable sequentially



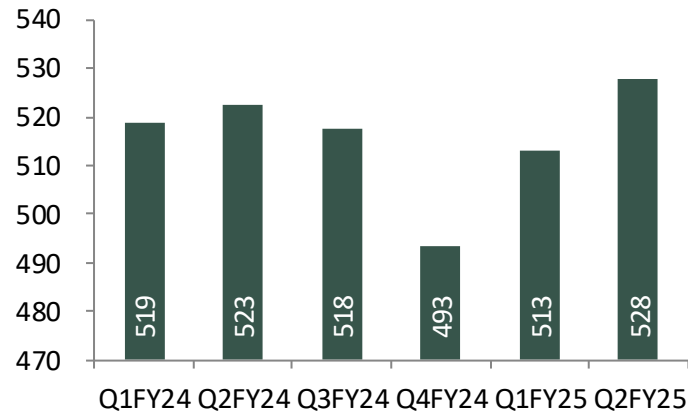
Source: Company; IDBI Capital Research

Exhibit 9: Deposits growth momentum moderated



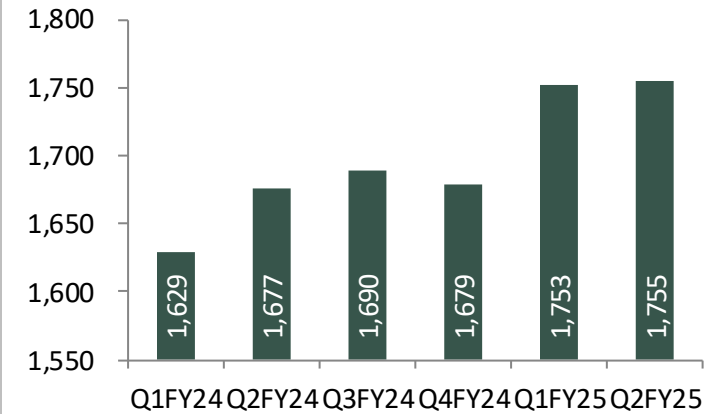
Source: Company; IDBI Capital Research

Exhibit 10: CASA per Branch



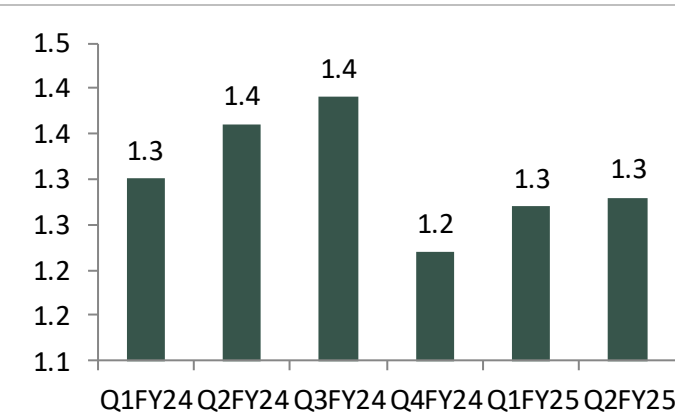
Source: Company; IDBI Capital Research

Exhibit 11: Deposit per Branch



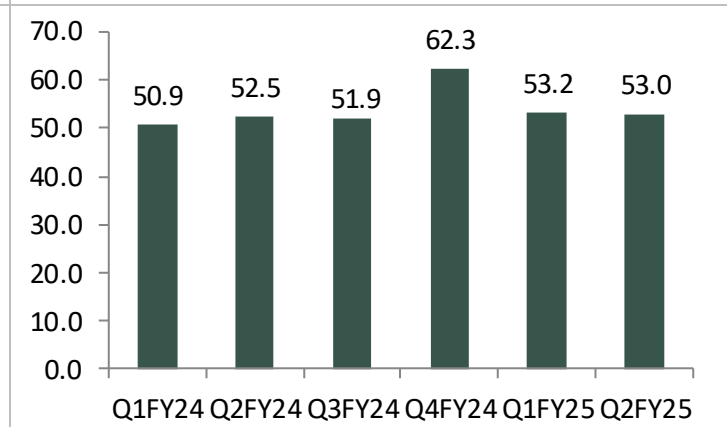
Source: Company; IDBI Capital Research

Exhibit 12: RoA were stable QoQ



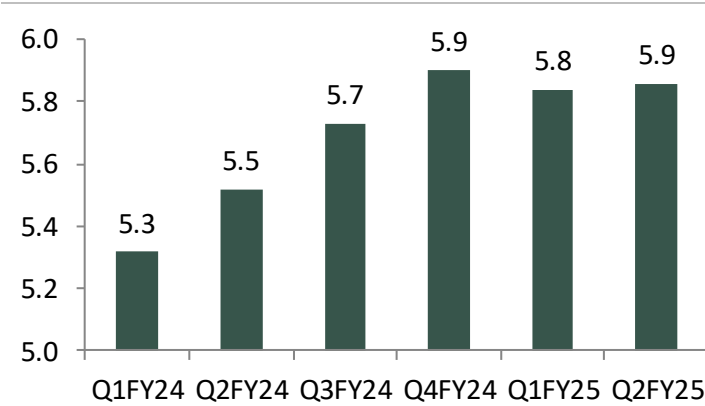
Source: Company; IDBI Capital Research

Exhibit 13: Cost to Income Ratio improved sequentially



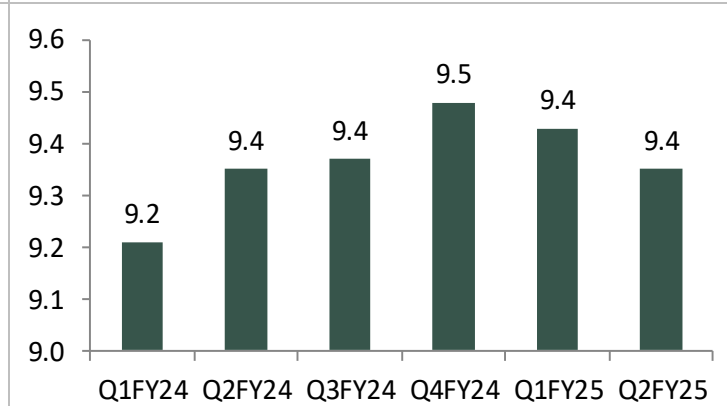
Source: Company; IDBI Capital Research

Exhibit 14: Cost of Deposits increased marginally QoQ



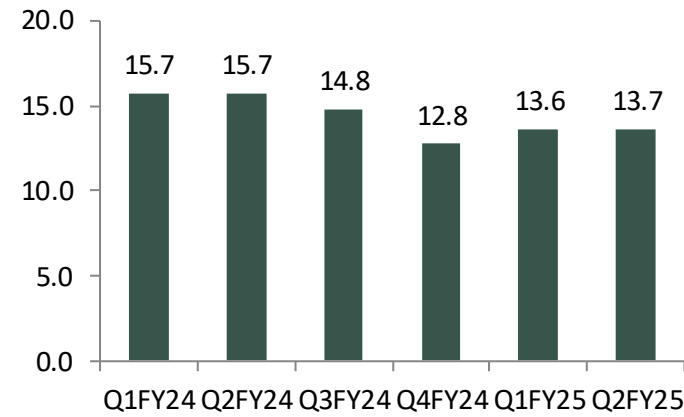
Source: Company; IDBI Capital Research

Exhibit 15: Yield on Advances declined marginally QoQ



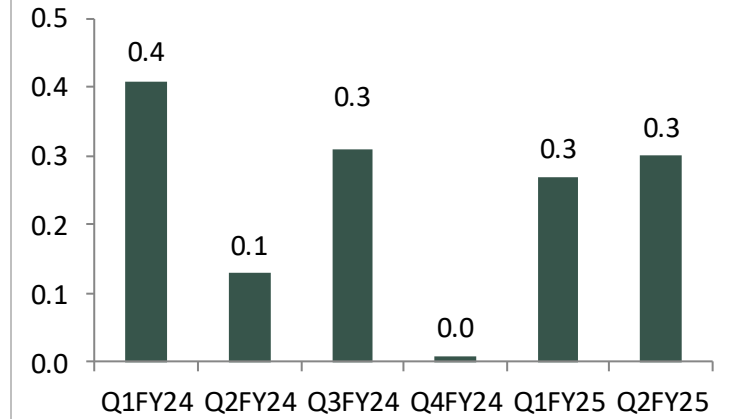
Source: Company; IDBI Capital Research

Exhibit 16: Return on Equity were largely stable sequentially in line with ROA



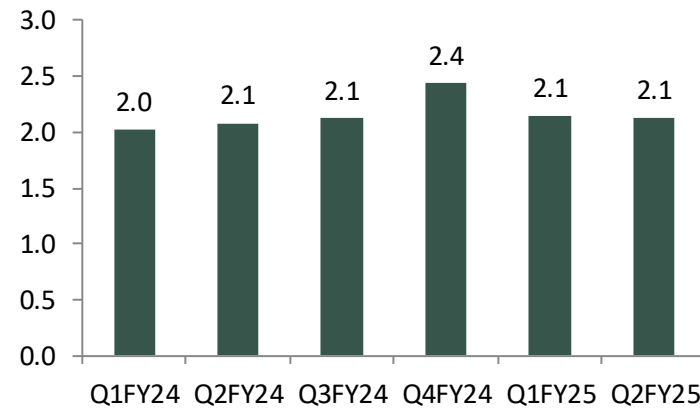
Source: Company; IDBI Capital Research

Exhibit 17: Credit Cost increased on a QoQ basis



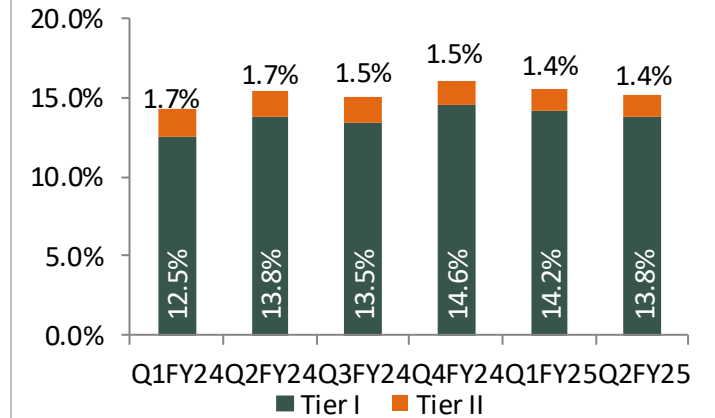
Source: Company; IDBI Capital Research

Exhibit 18: Cost to Assets remained stable QoQ

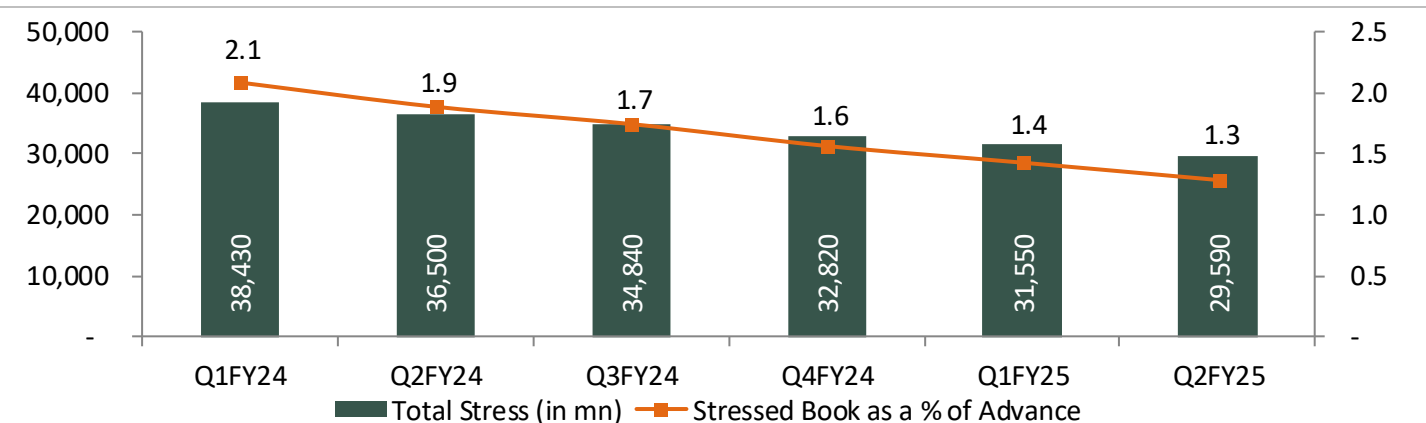


Source: Company; IDBI Capital Research

Exhibit 19: CAR remains comfortable



Source: Company; IDBI Capital Research

Exhibit 20: Stress Book continuing to witness improvement on a sequential basis

Source: Company; IDBI Capital Research

Exhibit 21: Composition of Slippages (Product Wise)

Slippages-Product Wise (In Mn)	Q2FY25	Q2FY24	Q1FY25	YoY (%)	QoQ (%)
Retail	2,490	1,940	2,390	28.4	4.2
Agri	880	540	710	63.0	23.9
Business Banking	630	680	620	(7.4)	1.6
CV/CE	110	70	120	57.1	(8.3)
Commercial Banking	170	420	330	(59.5)	(48.5)
Coporate Banking	-	-	-	-	-
Total Slippages	4,280	3,650	4,170	17.3	2.6

Source: Company; IDBI Capital Research

Exhibit 22: Movement of Slippages Ratio (In %)

Product Wise Slippage Ratio (In %)	Q1FY24	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25
Retail	1.92	1.27	1.29	1.16	1.29	1.30
Wholesale	0.18	0.19	0.56	0.10	0.78	0.76
Bank	1.12	0.78	0.96	0.68	0.14	0.07

Source: Company; IDBI Capital Research

Exhibit 23: Composition of Retail Advances (Product Wise)

Product Wise Retail Advances (In Mn)	Q2FY25	Q2FY24	Q1FY25	YoY (%)	QoQ (%)
Housing	2,93,630	2,64,540	2,87,250	11.0	2.2
LAP	1,31,070	1,08,920	1,23,860	20.3	5.8
Auto	-	45,370	-	-	-
Personal	82,560	63,010	78,000	31.0	5.8
Other	39,250	32,320	39,280	21.4	(0.1)
Total Retail Advances	1,27,890	1,05,930	1,22,550	20.7	4.4

Source: Company; IDBI Capital Research

Exhibit 24: Changes in Product Mix (Retail Advances)

Product Wise Retail Advances Mix (In %)	Q2FY25	Q2FY24	Q1FY25	YoY (%)	QoQ (%)
Housing	44	43	44	88 bps	-59 bps
LAP	19	18	19	187 bps	41 bps
Auto	-	7	-	-	-
Personal	12	10	12	209 bps	26 bps
Other	6	5	6	61 bps	-22 bps
Total Retail Advances	100	100	100		

Source: Company; IDBI Capital Research

Exhibit 25: Composition of Gross Advances (Product Wise)

Product Wise Gross Advances (In Mn)	Q2FY25	Q2FY24	Q1FY25	YoY (%)	QoQ (%)
Retail Loan*	7,15,330	6,43,340	6,88,820	11.2	3.8
Agri Loan	80,270	2,51,150	76,840	(68.0)	4.5
Business Banking	1,91,210	1,59,970	1,81,590	19.5	5.3
CV/CE	39,320	27,340	37,280	43.8	5.5
Commercial Banking	2,47,600	1,97,290	2,30,030	25.5	7.6
Corporate Banking	8,32,380	6,80,590	8,23,010	22.3	1.1
Total Gross Advances	21,06,110	19,59,680	20,37,570	7.5	3.4

Source: Company; IDBI Capital Research, *Retail loan includes MFI portfolio.

Exhibit 26: Changes in Product Mix (Gross Advances)

Product Wise Gross Advances Mix(In %)	Q1FY25	Q1FY24	Q4FY24	YoY (%)	QoQ (%)
Retail Loan	34	33	34	114 bps	16 bps
Agri Loan	4	13	4	-901 bps	5 bps
Business Banking	9	8	9	92 bps	17 bps
CV/CE	2	1	2	48 bps	4 bps
Commercial Banking	12	10	11	169 bps	47 bps
Corporate Banking	40	35	40	480 bps	-87 bps
Total Gross Advances	100	100	100		

Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY21	FY22	FY23	FY24	FY25E	FY26E
Net interest income	55,337	59,620	72,322	82,935	96,676	1,14,669
<i>Change (yoy, %)</i>	19%	8%	21%	15%	17%	19%
Fees	13,343	17,809	22,995	27,953	29,672	35,013
Other Income	6,244	3,082	305	2,840	7,289	7,729
Net Revenue	74,924	80,510	95,622	1,13,728	1,33,637	1,57,412
Operating expenses	36,917	42,932	47,678	61,983	71,954	83,032
Employee expenses	20,342	23,206	21,730	28,231	33,151	37,245
Other expenses	16,575	19,726	25,948	33,752	38,802	45,787
Pre-Provision Profit	38,007	37,579	47,944	51,745	61,684	74,379
<i>Change (yoy, %)</i>	19%	-1%	28%	8%	19%	21%
Provision	16,634	12,218	7,499	1,961	6,795	7,963
PBT	21,373	25,361	40,445	49,784	54,888	66,416
Taxes	5,470	6,463	10,339	12,578	13,815	16,717
<i>Effective tax rate (%)</i>	26%	25%	26%	25%	25%	25%
Net profit	15,903	18,898	30,106	37,206	41,073	49,699
<i>Change (yoy, %)</i>	3%	19%	59%	24%	10%	21%
EPS	8.0	9.0	14.2	15.3	16.8	20.3
Return on Equity (%)	10.4	10.8	14.9	14.7	13.2	14.0
Return on Assets (%)	0.8	0.9	1.3	1.3	1.2	1.3

Balance Sheet

(Rs mn)

Year-end: March	FY21	FY22	FY23	FY24	FY25E	FY26E
Capital	3,992	4,205	4,232	4,871	4,900	4,900
Reserves	1,57,252	1,83,733	2,10,830	2,86,073	3,27,933	3,72,733
Networth	1,61,244	1,87,938	2,15,063	2,90,944	3,32,833	3,77,633
Deposits	17,26,445	18,17,006	21,33,860	25,25,340	29,39,959	34,29,209
Current deposits	1,18,603	1,43,883	1,57,835	1,67,921	2,05,797	2,40,045
Saving deposits	4,68,523	5,30,827	5,43,370	5,78,587	8,52,588	9,94,471
Term deposit	11,39,319	11,42,296	14,32,656	17,78,832	18,81,574	21,94,694
Borrowings	90,685	1,53,931	1,93,193	1,80,264	2,79,163	3,43,787
Other liabilities	35,299	50,588	61,303	86,570	84,243	83,756
Total Liab. & Equity	20,13,673	22,09,463	26,03,419	30,83,118	36,36,198	42,34,385
Cash	1,95,913	2,10,103	1,76,887	1,89,629	2,30,168	2,39,219
Advances	13,18,786	14,49,283	17,44,469	20,94,033	24,70,959	29,15,732
Investments	3,71,862	3,91,795	4,89,833	6,08,595	7,16,602	8,29,266
Fixed Assets	4,911	6,339	9,340	10,201	10,711	11,246
Other Assets	1,22,201	1,51,942	1,82,890	1,80,660	2,07,759	2,38,922
Total assets	20,13,673	22,09,463	26,03,419	30,83,118	36,36,198	42,34,385

Financial Ratios

(%)

Year-end: March	FY21	FY22	FY23	FY24	FY25E	FY26E
Growth						
Deposits	13.4	5.2	17.4	18.3	16.4	16.6
Advances	7.9	9.9	20.4	20.0	18.0	18.0
NII	19.0	7.7	21.3	14.7	16.6	18.6
Pre-Provision Profit	18.6	(1.1)	27.6	7.9	19.2	20.6
Net Profit	3.1	18.8	59.3	23.6	10.4	21.0
Spreads						
Yield on Assets	8.0	7.2	7.8	8.6	8.7	8.7
Cost of Funds	4.8	4.1	4.5	5.5	5.7	5.6
NIM	3.2	3.2	3.4	3.2	3.2	3.2
CASA	34.0	37.1	32.9	29.6	36.0	36.0
Operating Efficiency						
Cost-to-Income	49.3	53.3	49.9	54.5	53.8	52.7
Cost-to-Assets	1.9	2.0	2.0	2.2	2.1	2.1
Asset Quality						
GNPA	3.4	2.8	2.4	2.1	2.1	2.2
NNPA	1.2	1.0	0.7	0.6	0.7	0.7
Provision Coverage	65.9	66.4	71.3	72.3	69.3	68.1
Credit Cost	1.3	0.9	0.5	0.1	0.3	0.3
Capital Adequacy						
CAR	14.6	15.8	14.8	16.1	14.7	14.3
Tier I	13.9	14.4	13.0	14.6	12.7	12.2
Valuation						
EPS	8.0	9.0	14.2	15.3	16.8	20.3
ABV	74.9	84.4	97.4	115.6	130.8	147.8
P/E	23.2	20.6	13.0	12.1	11.0	9.1
P/ABV	2.5	2.2	1.9	1.6	1.4	1.3
ROE	10.4	10.8	14.9	14.7	13.2	14.0
ROA	0.8	0.9	1.3	1.3	1.2	1.3
RORWA	1.5	1.6	2.2	2.1	2.0	2.1

Source: Company; IDBI Capital Research

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Key to Ratings Stocks:**BUY:** 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.**IDBI Capital Markets & Securities Ltd.****Equity Research Desk**

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